EXECUTIVE OFFICE
FOR
ADMINISTRATION AND FINANCE

OFFICE OF PURCHASED SERVICES

PURCHASE OF SERVICE REFORM:

FINAL REPORT

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PREFACE

The Office of Purchased Services has been asked to close as of January 31, 1990. We had determined, at the creation of the Office, that to be effective, the effort to reform the POS system had to be accomplished within a defined time period. Reform, to take place, needs a beginning and an end. If there is to be a continuation of POS reform, its integrity will rely on a freedom from "vested interests" or personal ambitions. We remain true to these principles and we do not recommend a "replacement" or continuation of OPS if it is to be a standing office, thereby adding another layer to an already overly bureaucratic system.

This is not to imply that POS reform is fully implemented or that there are not many tasks to be done to enhance and preserve reform. Rather, we rely on the principle that the participants of the system must have ownership of reform. Ownership brings with it the responsibility to move forward, to make things happen, and to safeguard the integrity and principles of the Reform Agenda. We are asking you to take up where we have left off.

Lack of candor is a major ill of the system. Throughout our tenure, consensus was difficult to achieve not because there was any disagreement about the nature of either problems or solutions (in fact, there was remarkable agreement) but because they were never "put on the table" honestly. This report reflects the candor we feel necessary to preserve the integrity of the reform.

INTRODUCTION

The Purchase-of-Service system in Massachusetts is vast, encompassing five secretariats, over twenty state agencies, and parts of the judiciary. It provides a broad array of over 250 types of programs, affecting the lives of at least a million citizens of the Commonwealth. It is currently funded by over $1 billion in state appropriations.

I. HISTORY OF THE PURCHASE OF SERVICE SYSTEM

Growth of the State's Investment in Purchased Services

The Commonwealth of Massachusetts has been purchasing human services for the past twenty years. During the past decade the volume of contracting has burgeoned, from $500 million in 1980 to over $1 billion in 1990. Today, POS is virtually the only mode of delivering community-based services in the Commonwealth today.

The decision to "buy" rather than "make" services was not necessarily a visionary policy decision ten years ago. The pressure to deinstitutionalize, from the Federal government, advocate groups, and several Federal court consent decrees, led to the decision to contract for services as a matter of expediency rather than a reasoned assessment that contracting was an effective means of service delivery. The obstacles offered by civil service and union rules, the difficulty in obtaining new state positions and the lack of state facilities in the community made contracting for services an appealing alternative to state-operated programs.

The fact that contracting was originally an expedient had far-reaching implications. Existing state policies, procedures, and systems were geared to direct service delivery and were applied uncritically to contract systems. Consequently, we treated providers more as subdivisions of state government than as independent entities. The same kind of direct budgetary and program controls were assumed to be appropriate for purchased services.

The Roots of the Provider System

Two decades ago there were relatively few provider agencies. Most of these were long-established, well-endowed "philanthropic" organizations. There were, however, an increasing number of groups, most often families of the disabled, whose advocacy created the pressure not only for deinstitutionalization but for more and better community services as well. The state encouraged these organizations to become direct service providers. Of the 1100 service

contractors in Massachusetts today, well over half are under ten years old. Thus, the origin of most provider agencies was grass-roots advocacy, not business entrepreneurship. This led to the providers' difficulty in conceiving of themselves as independent business enterprises, whose mission to serve clients sometimes came into conflict with their need to survive as a fiscal entity.

The Need for Reform

The past ten years has seen the growth of a contracting system which has been encumbered with bureaucratic procedures and paperwork. Such procedures are designed to achieve the same kind of control over provider entities as that which exists over state operations. This has resulted in micromanagment of contractors. Providers have sacrificed the fiscal viability of their agencies to serve more and more clients with inadequate resources. From the very best motives, the state and the providers community have both pursued strategies resulting in a fiscally fragile and inefficient system whose collapse would have devastating consequences for broad segments of the Commonwealth's citizenry.

This problem was not discovered recently. As long ago as 1980, the Massachusetts Taxpayers' Foundation issued a study of POS entitled "Can State Government Gain Control?" In 1984, after an extensive systemic audit, the State Auditor issued the "Blueprint for Reform", containing a set of recommendations for streamlining the system and reshaping accountability procedures. Finally, the FY 1986 Senate White Paper, "Protecting the Promise", mandated many new policy directions for POS. These reports represent a long history of efforts to reform the POS system; yet the system somehow continued to resist change.

II. THE REFORM EFFORT

The Establishment of the Office of Purchased Services

In May, 1987, the Office of Purchased services was established within the Executive Office for Administration and Finance in accordance with a legislative mandate contained in Chapter 206 of Acts of 1986, based on the Senate's "Protecting the Promise". The office was to "...implement a consistent, efficient and accountable system for agencies of the Commonwealth which contract for social and rehabilitative services..."

Staffing

Peter Nessen was recruited from the private sector to serve as the director of the new office, taking a three-year leave

of absence from his accounting firm, thereby creating a time frame in which reform was to be accomplished. Five staff were recruited with a variety of backgrounds: private consulting, rate setting, state contracting, public administration and provider management.

Operating Principles

An initial concern of the Office was to avoid fire fighting daily crises, so as to keep focused on the long-term needs of the system. In order to preserve a vision, the Office began by developing a set of fundamental principles to govern the purchase-of-service system (POS) and to guide its efforts. In a sense, these principles formed a "constitution" for the POS system, defining the fundamental and ideal attributes of the public/private partnership.

The most important of these principles was that client comes first. The second principle was that the "partners", state and provider, must recognize that the provider must survive as a business, in order to deliver its mission to clients. Only through a smoothly functioning purchasing system and a stable, financially secure and professionally sound provider community can clients be well served.

For OPS and other parties to the POS system, these principles served as a means to evaluate any proposed reform as well as measure the performance of the Office in implementing reform. OPS approved, supported or undertook only those policies, procedures or reforms which were consonant with these principles.

Strategy

Not only is the POS system large, complex, and diverse, it has an array of constituents with direct and legitimate interests in its successful operation. In addition to the "parties to the contract" - state and provider - there are advocate groups and clients' families, provider trade associations, the legislature, foundations and other funders, and private sector interests like banks who extend credit to providers. This complex arena demanded a thoughtful strategy to encompass the concerns of all interests and to reduce potential opposition to change.

The fundamental premise underlying the strategy was that consensus should guide the reform. The participation of interested constituents in assessing the system, developing a plan for change, and implementing reform was essential. The ultimate goal was a sense of ownership by all participants of the reform itself. On this basis, the Office adopted several tactics:

o Every opportunity to listen to the concern of the system's

participants, in assessing the problems and developing solutions, was used. One-to-one discussions, large and small group meetings, program visits, presentations and conferences, and ultimately, hands-on field tests of components of the reform plan, constituted the operations of the Office.

- All activities were conducted as an open process. Nothing was proposed or implemented without giving everyone an opportunity for input. This brought to the plan for reform the best ideas people had to offer, and resulted in an iterative process of refinement and improvement in the planning and implementation of the Reform Agenda.

- Although empowered to do so by legislative language, the Office resisted employing mandates or enforcement of change. Instead, the Office facilitated and coordinated consensus-building.

- The Office encouraged and exhorted participants to set aside immediate concerns and short-term self-interest in order to focus on long-term goals and to address issues generic to the system. This turned out to be the most difficult part of the reform process; the system seemed to be geared to crisis management and day-to-day survival.

III. ELEMENTS OF THE AGENDA FOR REFORM

General

The emphasis on control of service delivery through extensive reporting and paperwork requirements has had one unintended but calamitous effect: a loss of focus on the client. The resources, human and monetary, directed toward bureaucratic procedures, on both the state's and providers' parts, have resulted in fewer resources available for service delivery to the client.

Ironically, the paper chase has not led to greater accountability or control of service delivery. There is general consensus that the POS budget is a "black hole", where we may know something (but not much) about items of expense, but we know nothing at all about the product, the outcome, and most important, the effect of the program for the client.

From the broadest perspective, the Reform Agenda was designed to answer the questions: What did we get for the taxpayer's dollar? What was the outcome of the program? What benefits did the client derive?

The ultimate outcome of POS reform is to be able to measure performance, to determine what programs are effective for

client needs, and to describe and communicate the benefit of service delivery. The Agenda has several elements, each of which is necessary to achieve this goal but none alone is sufficient. These elements are interrelated and interdependent and must be treated, and implemented, as a whole.

The Contracting System: Regulations, Contracts and Procedures

The Need: The regulations governing the POS system had not been comprehensively reviewed for ten years; i.e. they were developed when the POS system was in its infancy. Over the years, provisions had been added in response to particular events or situations; the result was an illogical pastiche, with an accompanying body of policy and procedure which more often was developed to circumvent troublesome provisions of the regulations, rather than to insure compliance with law and statute. This "tangled web" required an army of well-versed technocrats to get from point A to point B.

The existing regulations also dictated an annual contract cycle. As the system increased in size and complexity, bureaucratic layers were added, paperwork increased, and the ability to evaluate the program was lost. All resources had to be devoted to pushing through contracts, estimated conservatively at 4,500,000 pieces of paper, each year.

Contracts, in theory the document which defines the relationship among state, provider, and client, came to be seen as technical filing requirements. No one wanted to read, much less enforce, contracts. Since the system allowed no means, time, or resources to evaluate performance, contracting had become a wasteful and hollow exercise.

The Response: OPS redrafted the regulations to simplify compliance and to allow more flexibility in contracting. The single most important feature of the new regulations was the five-year contract cycle. Two important objectives were achieved with this provision. First, it freed time and resources for developing good contracts, and to address the issue of performance and program evaluation. Second, the longer cycle recognized that the progress of clients should not necessarily be measured in 12-month periods.

The contract formats were completely revamped to direct the system's focus to the client. The contract's Program Description begins with a comprehensive client profile and a delineation of the goals and objectives which state and provider agree are appropriate for that target population. These goals then lead to the service activities deemed necessary for the client's progress. Service activities translate into resources - staff, program space, equipment, supplies, etc. These resources are then matched to prices (see Component Pricing), setting the funding level for the

program. Finally, the benchmarks of client progress are identified and the means of measuring performance become part of a comprehensive program evaluation system.

The Comptroller's expenditure reclassification project, revision of the state's chart of accounts, has offered even further opportunities to streamline systems and create new flexible contracting mechanisms. It will be possible to create a master contract procedure whereby the provider holds a single contract for a single program with one state agency, instead of multiple contracts with multiple agencies for the same program. Open order, or "blanket" purchasing has been streamlined to allow easier temporary or emergency purchase of services. In addition, a great benefit of expenditure reclassification will be the full and consistent accounting of the Commonwealth's true dollar investment in client services.

Finally, OPS has extended the EOHS Master Agreement system to all state purchasers so that a provider can execute one "boilerplate" agreement with a principal state agency, allowing contracts to focus solely on the program being purchased. The Master Agreement must be submitted only once, when the provider enters the POS system for the first time.

Yet to be Done: The POS regulations should be revisited periodically, to insure that they remain relevant in an evolving system and that we have not added back cumbersome and pointless requirements. The single "Master Contract" concept needs further development and implementation. Unified and standardized licensing, quality assurance, and program evaluation procedures, instead multiple, overlapping and duplicative processes administered by several state agencies, are possible and viable under a master contract system (See Appendix B). Such streamlining measures can yield significant cost savings to redirect toward service delivery.

Component Pricing

The Need: Rate setting for community-based programs was initiated in the late 1970's, modeled on the historical cost methodology then in use for hospitals and other large health facilities. The approach, administered by the Rate Setting Commission, was based on the audit of an individual provider's costs for each program and for the agency as a whole. The methodology required extensive and detailed annual financial reporting (RSC 1100 form) from providers. The costliness of this rate methodology led to significant consequences. As the system expanded from the few hundred individual program rates in the beginning of the decade to over 6000 rates today, resources did not keep apace. The result was that rates were simply not set (currently 85% of POS rates are negotiated between the provider and state

agency, with no Rate Setting Commission audit or review). For the few rates subject to the audit approach, most were set well after the commencement of the contract, wrecking havoc with state and municipal budgets.

Moreover, there are intrinsic problems with the historical cost approach. First, there was a powerful disincentive for cost efficiency. The prospective rate is based on expenditure: the higher the prior year's expenditure, the higher the future rate. Second, the spending pattern of a providing agency is constrained by both RSC and state agency policy. For instance there was at one time a policy that the general and administrative ("overhead") rate could not exceed 15% of program cost. We began to lose any sense of the true cost of service delivery as policies, not real cost, dictated spending patterns. Dozens of expenditures were subjected to this approach.

Third, the historical cost methodology had a more insidious effect. The prospective rate was based on historical cost plus inflation, by line item. The staffing, program space, etc., i.e. the program resources, had changed dramatically by the time the new rate went into effect. Flexibility, the ability to change program design, to respond to changing client needs, was one of the very rationales for purchasing services. For the historical cost approach to work well, programs had to maintain a static configuration. As both state and provider acknowledged the need to change the program, "negotiated rates" became the alternative to historical cost. However, negotiation was based on no "true cost" information and a blizzard of forms, in addition to detailed financial reporting, were laboriously completed every year for every contract, in order to reconcile historical to current program design and to available funding levels.

The Response: OPS designed a completely different approach to pricing. First, observing the principle that "price must follow program" (corollary to "the client comes first"), the system was designed to be absolutely program-neutral. Contract negotiators first develop the components of the program (the resources), based on the agreed goals and objectives, then match the prices to those program components. Thus, program performance and funding level of the contract are integrated.

Second, based on the principle that a providing agency is a business enterprise, price ranges for individual components were based on the current market value of any required resource, since the provider must purchases such resources in the "real world". We should no longer assume that philanthropic activities can be conducted in church basements, that residential programs must sited in marginal neighborhoods, or that "virtue is its own reward" and human

service workers can somehow put food on the table without adequate salaries.

Third, to deal with the long-neglected problem of low staff salaries, OPS developed salary standards based on the principle that reduction of staff turnover is a desirable aim for continuity of care and for overall program performance. Therefore, direct care salary levels are correlated to staff turnover and vacancy levels. A state agency may choose to negotiate low salary levels with a provider; however, performance expectations must be adjusted downward to account for high turnover and long-term vacancies in program staffing (the current average direct care turnover is 66.7% annually).

Finally, the component pricing system is inexpensive to administer, can produce timely price information, and is easy for providers and state agencies to use. The RSC 1100 has been eliminated for most of the system and replaced with a streamlined reporting document which fulfills the need for fiscal accountability from provider agencies.

Yet to be Done: The component pricing system should be implemented for Fiscal 1992 recontracting. The concept, the approach, and the first Pricing Catalogue are all in place. OPS has proposed a new administrative entity for pricing, auditing, and management information systems. This proposal is contained in Appendix A.

The state budget process, which currently regards and treats the POS portion of the budget as the "black hole", should be revamped to assess budget needs in the context of component prices. The assumption that component pricing will make POS a "budget buster" like Medicaid is erroneous. We must invoke common sense and realize that the state should only be buying what it can afford. When we purchase pencils, we buy only the number of pencils we can afford, of a quality that is functional. We would never consider trying to buy half a pencil or beating down the vendor's price so that he/she goes out of business. Similarly, for the POS budget, we should be buying the quantity of services we can afford, of a quality that is functional, at the "real world" price. The POS budget must be built up from the rates adequate to maintain service delivery. The number of units purchased is the variable which allows us to live within the limits of state appropriations.

Uniform Financial Reporting

The Need: There is, of course, a need for proper fiscal accountability. The principle purpose of such accountability is to provide the system with current, reliable information regarding the agency's fiscal status and the results of its operations.

The Response: To meet this need and guided by the input from the Attorney General's Office, State Auditor, secretariats, agencies, providers, foundations, and the CPA community, OPS developed a single standard financial and statistical report, the Uniform Financial Report. This report is subjected to an independent CPA audit, which assures basic fiscal accountability and compliance with laws, statutes, and accounting standards. The simplicity of the report leads to cost efficiencies in provider operations; the CPA audit eliminates the need for multiple, often duplicative auditing functions within the state.

This new report has had several benefits:

- o Freeing personnel and other costly resources of all parties concerned;
- o Improving coordination though the use of a standardized, uniform, and universal financial database;
- o Streamlining and simplifying fiscal accountability to allow more focus on programmatic accountability.

Yet to be Done: The Uniform Financial Reporting system should be extended to all community-based providers such as 766 schools, community mental health centers, and ICF-MR providers. This will allow the maximum streamlining effect, eliminating multiple and onerous reporting requirements for providers.

Fiscal Capitalization

The Need: Most providing agencies suffer from undercapitalization. Over 25% of the providers are technically insolvent. This condition threatens the very survival of the provider and thereby, the continued delivery of services. Adjusting downward next year's rate paid by the state absorb any surplus resulting from managerial efficiencies. The provider begins every year as a financial start-up, facing the same risks that any start-up company incurs. This makes the provider system vulnerable and fragile.

As a result, there is a pervasive inability of providers to acquire fixed assets or accumulate working capital - the very resources necessary for any business entity's survival. Moreover, this is a costly way of doing business. Not only are we constantly bailing out providers who are in a chronic deficit position, we also force expensive leasing solutions for facility and equipment needs, instead of encouraging capital acquisition.

State funding now accounts for 85% to 95% of the typical provider's budget. The dramatic growth in public purchase-of-service has led to an equally dramatic shift away from voluntary contributions and private support towards

state reimbursement as providers' primary and often, sole source of operating revenues. This dependency makes the provider hostage to the state - the relationship ceases to be a partnership. The lack of diversification of funding also makes the provider financially vulnerable. The solvency of these organization is vulnerable to the vagaries of state tax collection.

When the Commonwealth purchases services, it is buying the providers' expertise in managing programs. Yet, when providers are obligated to adhere to a 95 line-item budget, they lose the flexibility they need to manage effectively. This is symptomatic of the state's attempt to control service delivery by micromanagement of providers. In addition, overwhelming reporting requirements and a host of disincentives to save money create costly inefficiencies. There is no doubt that we have spent money unwisely in POS, resources better spent on direct care.

The Response: Since provider insolvencies stem predominantly from inadequate rates, OPS' market-based component pricing system, by adequately funding operations, will help providers finance and replace capital assets from internally generated funds. Under component pricing, the line item contract budget is eliminated. Giving the rate as a single price should allow providers the flexibility in managing programs to achieve the best results for clients.

Shared Service Corporations: The system must begin to explore new business practices that can nurture the new or smaller provider who is effectively delivering community services. Over 53% of the provider community falls into this category.

OPS has proposed the concept of Shared Services Corporations which will consolidate the accounting and non-program functions of several providers. The system will be able to maintain the numbers of small providers and the advantages they bring to service delivery while creating efficiencies in non-program costs. By creating economies of scale in administration, the small provider will be able to compete better with large providers in competitive procurement.

Capital Acquisition: OPS helped facilitate debt financing available to providers by participating in the development of tax-exempt bonds pools, allowing providers access to traditional sources of capital not previously available to them and in this case, offering through Massachusetts Industrial Finance Agency 100% financing for capital acquisition.

Yet to be Done: The total reliance upon the Commonwealth funding should be reduced. The system must begin to leverage state funding with traditional and creative outside sources of support. This effort must be rewarded by incentives, like

revenue retention, to those who are willing to seek these outside sources of revenue. Providers and purchasing departments, alike, must aggressively collect sliding fee scale payments, third-party payments, federal financial participation and fund raising to augment state support.

Further cost efficiencies can be achieved by allowing advance payment to providers, as the federal government does. OPS estimates that such a measure would save as much as $20 million in the cost of providers' short-term borrowing.

The Creation of a Profession: Vision and Visibility

The Need: There is a continual need to enhance the sense of profession. A profession that brings together the individual human service provider, academics, clients and their advocates, funders, the business sector, the Commonwealth and other stakeholders to address issues of human service policy and practice.

The Response: This need is addressed by the creation of the Institute for Community Services. The Institute's mission is to:

- create long range policy;
- develop standards for professional conduct and practice accreditation;
- conduct peer review;
- develop program performance objectives
- coordinate research;
- conduct continuing professional education;
- develop strategies for improved recruitment and retention of personnel;
- promote professional identity, integrity and reputation; and
- advocate change, e.g., a fair price for a quality service delivery to a client.

Yet to be Done: The activities of the Institute need the participation and support of all of the constituents of the POS system, to enable it to address these generic concerns.

Performance-Based Contracting

The Need: The fragility of the POS system, the lack of rational budget development, the lack of a sense of profession, all represent symptoms of a greater underlying problem: The system's participants are unable to describe their product. What is the benefit of the program for the client? Which programs are effective and which are not? The answers to these questions represent the most important aspect of the system's accountability.

The Response: OPS has not prescribed a system of performance

measurement. Only when the system comes to focus on the client, when contracts emphasize client-based goals and objectives and evaluation of client progress, and when resources to achieve performance are adequately priced and funded, can we expect superior performance. This, the culmination of reform, must be an evolutionary process.

Yet to be Done: As the elements of reform are implemented, efforts to move toward performance-based contracting should begin to take shape. The development of performance systems must be a cooperative venture among the POS constitutents. Such systems must include incentives for good performance and should be supported by well-developed information systems. Care must be taken not to create new complex and burdensome bureaucratic procedures which only again divert resources and focus from service delivery to clients.

IV. CONCLUSION

We in the Office of Purchased Services are content that our two and a half years of effort have been on the right track, that the Agenda for Reform put together the most creative thinking from the best minds in the POS system. Most important, we think that it will insure that clients are well served. Beyond the immediate implementation of the elements already described, there are several other initiatives which will support the institutionalizing of reform and the integrity of the Agenda.

RECOMMENDATIONS

Broadening the Scope of Current Initiatives

- o Uniform Financial Reporting should be extended to all social service providers, including chapter 766 providers, community mental health centers and intermediate care facilities for the mentally retarded, in lieu of existing reporting requirements, by legislative mandate in FY 1991.

- o Component pricing should be extended, by legislative mandate, to all social service providers, including chapter 766 providers, community mental health centers and ICF-MRs, in FY 1991.

- o Purchase-of-service procurement regulations should be comprehensively revised and/or developed to match the new expenditure classification categories created by the Comptroller and to achieve maximum efficiencies in procurement, authorization, and administration.

- o The Legislature should require, in statute, that no licensure or quality assurance regulation may be adopted without a prior assessment of its cost impact and

corresponding departmental, secretarial or legislative plan for funding any additional costs.

- The Administration and Legislature should revamp current POS budget procedures to take full advantage of component pricing by developing a "bottom-up" budget process which allows funding decisions to be based on program efficacy and on true price. Coupled with this should be a system-wide needs assessment and a mandated sunset review of all program types on a periodic basis.

Maximizing Efficiency Through Reorganization

- The establishment of component pricing and Uniform Financial Reporting allows the creation a single, central authority consolidating and integrating scattered and duplicative pricing, auditing and data processing functions. This initiative is described in attachment A.

- Current program reporting and assessment procedures are overlapping, duplicative, and costly. Attachment B details an OPS proposal to consolidate all social service program licensure in a single, central authority which will also coordinate and integrate other reporting, monitoring, and assessment procedures with the five-year contract cycle.

- The shift to five-year contracts and the focus on program performance should result in less paper processing for contract managers and more work for program monitors. In the longer term, the Institute for Community Based Services should eventually act as the major resource for quality assurance and provider prequalification. Accordingly, the Administration and Legislature should commission a comprehensive review of current staffing patterns throughout the POS system.

Investing in POS Reform

- The Commonwealth should develop a long term plan for financing of current POS services. This plan should take into account the additional revenues and savings made possible by POS reform as well as the recommendations set forth below.

- The Administration and the Legislature should require, as a precondition to the authorization of new or expanded program commitments, departmental assessments of and implementation plans for access to all possible sources of funding for POS services.

- The Administration and Legislature should agree that fully funding existing services are the first priority for new

revenues.

- The Legislature should encourage departments to maximum federal reimbursement by establishing retained revenue accounts for all departments and developing an incentive policy authorizing the use of any revenues beyond budget targets to invest new revenues in fully funding existing services.

- A similar incentive program should be developed to encourage private providers to maximize available third party revenues and fee collection.

- The Administration should develop and adopt a universal sliding fee scale for use in all publicly supported social service programs. Except in the case of entitlement programs, service recipients should be required to pay for service in accordance with their financial means.

- The Legislature should repeal the statute which requires all services rendered to the Commonwealth be paid in arrears, in effect, barring advance payment. Advance payment would dramatically reduce providers' reimbursable interest expense on borrowed working capital.

- The Legislature should allow and encourage health insurance coverage for less expensive and more appropriate alternatives to in-patient hospitalization. Many such programs are currently 100% funded by state appropriations and are utilized by clients who are otherwise insured.

- There should be systemic incentives for the creation of shared service corporations whereby small providers can achieve economies of scale in overhead operations.

APPENDIX A

PROPOSAL FOR A POS ADMINISTRATION

EXECUTIVE SUMMARY

RECOMMENDATION: The establishment of a POS Administration with system-wide responsibility for pricing, auditing, and data base systems.

Scope of Authority: Pricing and auditing authority over POS activities in all Commonwealth secretariats and agencies totalling over $ 1 billion, or over 12% of the state budget.

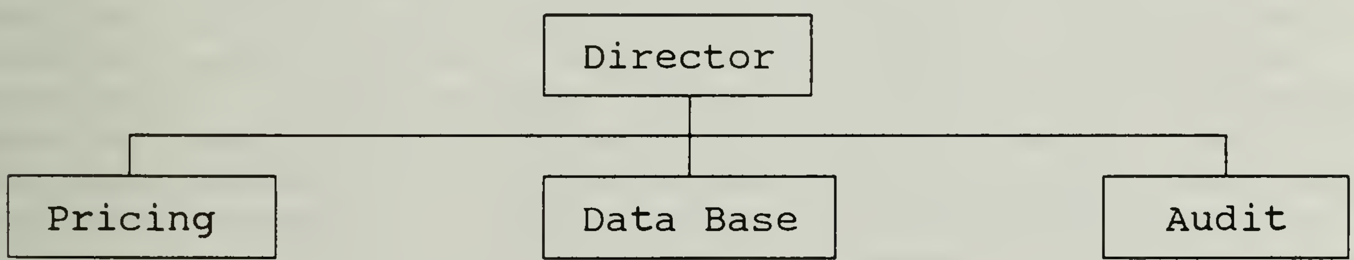
Location: An independent entity housed in the Executive Office of Administration and Finance or the Office of the Comptroller.

Resources: POS Administration will cost $958,000 which will be more than offset by savings realized through the elimination of existing offices. In fact, the net savings of this reorganization to the state is over $3.1 million.

Implementation: This office will be, overall, a "turnkey" operation, since most of its systems have been or will be implemented by OPS prior to FY 1991. Only the data base system requires a development process. It can begin operation by July 1, 1991 or earlier, if statutory impediments are overcome.

First Steps: Establish the POS in budget language and make corresponding adjustments to appropriations. Modify Rate Setting's enabling statute. Assess potential for corresponding efficiencies in agency contract management.

Organizational Structure and Functions:



o Market Survey o Data Collection o Audits
o Personnel Survey o Data Analysis o Quality Control
o Cost Analysis o Report Devel. & o Finan.
Standards: o Price Update Dissemination
Devel.& Enforce

INTRODUCTION

The current configurations of pricing and auditing functions, including MIS support, are fragmented, duplicative and costly. For example, there are audit operations in nine different agencies within state government. Each has a different mandate, scope of authority, and set of concerns, with minimal information sharing among them. This means that the POS system, consisting of 1,100 providing agencies, is subjected to multiple audits, none of which are guaranteed to be comprehensive, on one hand, or nonduplicative on the other. Even more inefficient is the rate setting system for social rehabilitative services which has not functioned to set "fair, reasonable, and adequate rates" for over 85% of POS for the past several years, yet 27 state positions continue to be ostensibly devoted to this purpose.

This situation leads us to propose some fundamental reorganization within state government to eliminate overlap, duplication, and fragmentation of POS administration and to insure streamlined and enhanced accountability. Our proposal is to combine existing resources and to integrate auditing, pricing, and information support functions into a single administrative entity, with oversight authority in these areas for all purchase of service activities in the Commonwealth. This proposal should not only make POS administration more effective but should also result in important cost savings.

ANALYSIS

PRICING

Last year OPS conducted a survey of state and provider staff involved with POS, to assess respondents' communication and decision making participation, perceptions of the current and proposed contracting policies and areas of consensus and tension among purchaser and provider fiscal and program personnel. In the survey, current rate setting procedures used by Bureau of Educational, Social, and Mental Health Services (BESMHS) of the Rate Setting Commission were among the most frequently cited sources of dissatisfaction and frustration with the POS system. Moreover, when respondents were asked to rate the relative fairness of 22 POS policies/procedures, rate setting received the lowest score by both state and provider respondents. The inability to establish fair rates, delays in setting rates, and burdensome reporting requirements for no ostensible purpose have lead to BESMHS' poor reputation.

It is simply not feasible, let alone cost effective, for the Commission to set individual program rates based upon a

detailed historical cost analysis for the 6,000 or more contracted programs offered by 1,100 provider agencies. According to a recent report from EOHS' Office of Auditing and Accounts, BESMHS sets only about 597 program rates a year (out of 6,000 programs) and of these, nearly 200 are class rates. Only 40 Chapter 766 providers have annual rates set on the basis on field audit. Audited historical cost pricing would be immensely costly to apply to the entire system.

OPS' "component pricing" initiative aims to create a rate setting system that is objective, fair, and efficient. The system is based on the fact that each individual program is composed of a set of components common to all programs. Rather than "pricing out" each unique program, a pricing authority could develop a range of standard prices for each of a comprehensive yet manageable set of optional program components. Then, the pricing of an individual program would simply involve matching component prices with the specific program components upon which the purchaser and provider have agreed.

The component pricing system requires a dramatic shift in the role of rate setting away from desk audit of historical costs and towards market research and statistical analysis. This, in turn, means a radical change in appropriate staffing: fewer accountants/auditors, more economists, statisticians and data processing staff.

Staff positions in the Commission's BESMHS Bureau total 27. Additional staff are assigned, from the Bureaus of Ambulatory and Long Term Care, to develop rates for certain Medicaid reimbursable social services such as mental health center outpatient treatment and ICF-MRS and, of course, the bureaus draw proportionately upon the Commission's data processing, legal and administrative resources. Collectively, these amount to at least 12 additional positions, bringing the number of staff devoted to setting social service rates to 39. In contrast, an independent pricing system should require a staff complement of 6 positions, with proper data base and audit support. Implementation should also result in significant reductions in departmental and provider resources currently devoted to review and reporting.

AUDITING

Auditing is one of the major tools for accountability in the POS system. Over the past several years, the POS system has witnessed an increased focus on and growing sophistication of POS audit and corresponding increased audit activity. It is certainly in the public interest and in the interest of the contract system to maintain and enhance this function.

However, audit activity has not only become fragmented, but audits are currently being conducted for purposes other than "keeping the system honest." As explained in the previous section, audit for the purpose of setting rates, for example, is neither desirable or efficient. In other instances, state agencies may be auditing only a single provider program or use of funds from a single funding source, also an inefficient use of resources. What is called for is a unified approach to audit, coupled with a new protocol to target audits to problem areas in the system.

OPS has already laid the foundation for streamlined and enhanced audit operations. The introduction of the Uniform Financial Report system this year opens the door to a unified audit approach. The Uniform Financial Report replaces the multiple financial reports providers have been required to submit annually to state and other funders. In addition to streamlining and simplification, the reporting system has numerous other benefits. Instead of providing financial information which is then subject to audit, the report itself is audited independently by the CPA. It contains a single uniform chart of accounts, insuring that the state and other funders have basic necessary information about a provider's operations. The form itself satisfies governmental auditing standards and requires compliance with internal control standards and with specific laws and statutes.

Thus the stage has been set for a consolidated, unified approach to post-audit. The independent CPA audit establishes a baseline accountability of providers' use of funds. Enhancement of this basic accountability comes through the creation of a "profile" system, generated from an automated financial database, of provider financial operations against which each providing agency will be measured. The "exception" provider is then targeted for post-audit. This focused approach allows us to allocate audit resources toward problem providers while having reasonable assurances that the rest of the system is operating well.

The siting of the audit operation in the Executive Office of Administration and Finance creates both administrative efficiency and enhanced objectivity. Since the audit unit will oversee all POS activity in the Commonwealth, the current duplication will be eliminated. Since it houses no contracting functions and has no direct interest in specific contracts or individual providers, its objectivity, essential to the audit function, will be increased.

Finally, there is a lack of capacity in the system to insure quality, uniformity, and compliance to standards in providers' audited financial statements. Development, maintenance, and enforcement of system-wide standards will be a important new function of the audit unit.

POS DATA BASE

The POS system over the last 20 years has been shaped by anecdotes. The negative public perception of the system has resulted from the occasional news headline and a complete lack of objective information about the system and what it accomplishes. Inside state government, budget and policy makers have been faced with the "black hole" of POS activity, frustrating their attempts to make rational resource decisions or develop reasonable management systems.

The first step toward creating a POS data base to serve the needs of a multiplicity of potential users inside and outside government is the information about providers' financial operations contained in the Uniform Financial Report. As demonstrated above, this data base creates the ability to target audits efficiently. It also leads to a capacity to develop financial standards for viability and soundness which are appropriate to our provider industry. Such standards will be the foundation for a credible determination of an individual provider's capacity to do business with the Commonwealth - thus, development, maintenance, and enforcement of prequalification standards will be a new capacity of the POS system.

The financial data base also provides essential support for the pricing process, allowing in-depth analysis to keep the component cost standards current. As the data basis becomes increasingly sophisticated, the pricing function will become increasingly efficient.

The most important function of the data base ultimately will be to provide decision support for budgetary and general policy making, defeating finally the power of the anecdote. There is a particular need for analytic information in the POS budget development process, in order to make sound decisions about resource allocation. Potentially there are a host of users of this data base, purchasing and overhead agencies, legislative offices, private funders and advocates, whose functions and activities rely on consistent, timely and reliable information. Although there are increasingly sophisticated information systems at the departmental and secretariat levels, there is no uniform system-wide data. The data base can expand far beyond basic financial information, to contain program data related to quality concerns and performance. It has the potential to answer the most important question we all need to answer: What did we get for the taxpayer's dollar?

RECOMMENDATION

The establishment of a POS Administration with system-wide

responsibility for pricing auditing, and management information systems.

Scope of Authority: The Administration would have pricing authority over all activities currently overseen by BESMHS, as well as new contracts coming into the POS ("M") subsidiary as a result of the Comptroller's expenditure reclassification and will encompass all secretariats. We also recommend that rates now set by the Bureaus of Long Term Care and Ambulatory care for mental health center services, homemaker services and ICF-MRs be transferred to the jurisdiction of the POS Administration to maximize the efficiency of component pricing.

Audit policy and procedures will apply to all private providing agencies delivering social rehabilitative services through state-funded purchasing arrangements. The Uniform Financial Reporting system and the scope of the data base will encompass the same population.

Location: Ideally, the Administration would be situated within the Commonwealth's organizational structure so as to encompass purchasing activities across agencies and secretariats. The Executive Office of Administration and Finance or the Office of the Comptroller are possible sites.

Resources: Resources made available from eliminating existing offices/functions far exceed the funds needed for the POS Administration. We suggest that the Office of Audit and Accounts (OAA) currently sited within the Executive Office of Human Services be transferred to the new entity, since its current operations are similar in function and scope to the anticipated audit unit, although its scope of authority would, of course, be expanded to the entire POS system. A data base system could possibly be developed within existing attributes and functions of the MMARS system. There may also be existing personnel at BESMHS with the prerequisite skills for the new pricing system.

Implementation: Through the current efforts of OPS, EOHS, and RSC, the pricing system will be in place for FY 1991 recontracting. As mentioned above, EOHS/OAA is already functioning similarly to the unit we propose and will await only the data base system to be fully operational. With most functions already established, the first job of the pricing unit will be to focus on the organizational and operational issues of system maintenance and integration of contracting, data base and audit. The data base development is basically a "build-from-scratch" effort but can possibly piggyback on existing systems.

First Steps: Include language establishing the POS Administration and corresponding appropriation adjustments in FY 1991 House 1. Create an enabling statute for POS

Administration and eliminate reference to social and rehabilitative services in the statute governing the Rate Setting commission. In addition, we recommend that a "model" staffing pattern be developed for contract management functions within purchasing agencies, creating parallel efficiencies by eliminating unnecessary operations, and that adjustments be made to budgets and personnel accordingly.

APPENDIX B

A PROPOSAL FOR CONSOLIDATED LICENSING & PROGRAM ASSESSMENT

INTRODUCTION

During the enormous growth of the Purchase of Service system in Massachusetts over the past decade, there has been a corollary growth of program licensing and, to a lesser extent, quality assurance systems. These function to assure both government and the public that the programs we fund are both safe and appropriate for clients. Currently there are over 5,000 community-based programs run by 1,100 providing agencies, at least 50% of which are systematically licensed according to departmental licensing standards and/or regulations. Quality assurance systems are less well developed but have been implemented in some agencies. In addition, there are numerous national accreditation systems, like CARF, JCAHO, and CWLA, in widespread use.

PROBLEM

Like many of the other policies and procedures for the purchase of service system, program licensing and quality assurance systems have developed in a fragmented, almost random fashion, in a vacuum of coordination or system-wide parameters. A legitimate concern of purchasing agencies is their own accountability for the health and safety of clients in their care or custody, leading to departmental licensing and other program assessment systems but also resulting in a "crazy-quilt" of duplicative and overlapping standards and procedures applied to some programs and no assessments applied to others. It is not even clear what criteria are used to decide whether a program should be licensed or not.

As providing organizations have grown to meet the capacity demands of the burgeoning POS system, they have entered into contracts with multiple departments. Over 35% of contract providers (excluding day care) do business with more than one department, the average agency delivering 4 different programs with 07 funding alone (inclusion of Medicaid and 766 programs probably doubles this number). This means that the majority of providers are subject to multiple licensing, certification, and/or quality assurance procedures, involving at least annual surveys and more frequent monitoring and reporting. A single program could conceivably be subject to three or four annual reviews, each of which may assess the program according to similar criteria. In addition, some departments also require program or provider accreditation or providers may seek such accreditation on their own. These accreditation often cover the same ground as licensing and/or quality assurance.

Moreover, there is not always a clear distinction between licensing (threshold) and quality assurance (aspirational) standards. Thus, even within a state agency's sets of program standards, there may be duplication and overlap. Nor have standards necessarily developed with an eye to effectiveness. For instance, staff credentials may be required which bear no relation to actual job responsibility or to client need (and may lead to unnecessary cost). Most current standards measure "process" as opposed to "outcome", so even with multiple procedures, we are still not able to ascertain the efficacy of our programs, much less make resource decisions on this basis.

The large purchasing agencies maintain large complements of licensing staff and sometimes quality assurance staff as well. A large part of the resources of the Office for Children are devoted to licensing. In addition, where accreditation is required, we reimburse providers for the cost through their rates.

Finally, there has been no system-wide assessment of program types which are not currently licensed, accredited, or otherwise formally assessed. Thus, while we experience overkill in some program areas, other areas remain unexamined.

RECOMMENDATIONS

To take effect in FY 1991, we propose the same approach which has already been proven successful in solving the duplication and fragmentation of providers' financial reporting requirements, resulting in the Uniform Financial Reporting system. This involves the examination of the entire body of departmental licensing, quality assurance, and accreditation standards, policies and procedures for duplication and overlap, resulting in a single set of baseline standards for health and safety concerns. Supplemental standards would then be developed to address specific areas in program types or individual concerns for different target populations. National accreditation systems should be examined for depth and scope of standards of excellence and where programs already undergo accreditation, a "deemed status" given. Where there are no such systems, standards of quality should be developed and implemented.

To take advantage of this unified approach to achieve maximum efficiency, resources now devoted to licensing and other program assessments should be brought together in a single state office, sited within the Executive Office of Human Services. Procedures should address the survey and assessment of providers as a whole entity, i.e. periodic licensing et. al. should be undertaken for all programs of

a providing agency at one time, using the baseline standards as well as the applicable supplemental program-specific standards.

Finally, a cycle of monitoring and assessment procedures should be built in the five-year contract so that licensing surveys can alternate with quality assurance or accreditation reviews, leading to a comprehensive evaluation using the results of all these processes toward the end of the five-year term. It is also an opportunity to standard and streamline some of the reporting requirements providers are subject to, including eliminating those not directly related to program assessment, client monitoring, or reimbursement.

FIRST STEPS

1. Survey existing regulations, standards, and policies and assess current levels of resources currently allocated to these activities (some of these information will be provided by the implementation plans required by Secretary Lashman in his April 26 memo approving five-year contracts. Survey numbers of programs currently licensed, certified, or accredited against each set of standards.

2. Create a set of unified health and safety standards and program-specific supplements. Use existing accreditation systems in lieu of state-operated quality assurance systems. Where quality assurance systems are developed, require standards and measurements oriented toward efficacy and performance.

3. Assess cost savings from and resource needs for implementation. Assess cost of licensing regulations through component pricing and feed information into budget process.

3. Develop appropriate enabling legislation for a consolidated single state licensing/quality assurance entity. Make adjustments to appropriations and transfer departmental staff.

4. Create implementation plan for coordinated program assessment and integrate into five-year contract cycle.

5. Link program assessment and evaluation information to the provider financial data base to create a comprehensive, system-wide information system. Create simplified "all-purpose" reporting format and eliminate unnecessary reporting.